National Agricultural Marketing Council
Strategic positioning of South African Agriculture in dynamic global markets

agriculture
Department:
Agriculture
REPUBLIC OF SOUTH AFRICA

INTERNATIONAL *TradeProbe*

No. 16, April 2009

TradeProbe is a joint initiative by the NAMC and the Department of Agriculture's Directorate: International Trade. The aim of this initiative is to create knowledge of trade-related topics by discussing/reporting trade statistics, inviting perspectives from people working in related sectors, reporting on trade-related research and stimulating debate.

THIS ISSUE OF TRADEPROBE COVERS THE FOLLOWING TOPICS:

- Overview of the WTO trade policy review body report and trade related development aspects on agriculture
- South African agricultural trade relations with India
- South African food inflation link with Chinese food imports

1.1 OVERVIEW OF THE WTO TRADE POLICY REVIEW BODY REPORT AND TRADE POLICY RELATED DEVELOPMENT ASPECTS ON AGRICULTURE[1]

Introduction

In an effort to assist the Trade Policy Review Body (TPRB) to undertake an annual overview of developments in the international trading environment the Director-General, Mr. Pascal Lamy, regularly prepares a report called for in Paragraph G[2] of the Trade Policy Review Mechanism (TPRM). A current copy of this report was published on 26 January, 2009. This section briefly highlights aspects of economic volatility and trade-related development aspects with regard to agriculture that have occurred since the third quarter of 2008 because of, or in the context of, global financial instability.

Widespread reference has been made over the past few months to the severe economic difficulties that would be caused in current circumstances by any significant resort to trade restricting or distorting measures in an attempt to protect businesses, jobs or farm incomes from the effects of the global economic growth slowdown. This would only worsen the economic situation for all and diminish prospects for an early economic recovery. Protectionism could also provoke retaliatory action by others that would compound the damage caused. Moreover, the risk of increased protectionism exists as long as there is still significant scope for WTO Members to increase their applied levels of tariffs and trade-distorting subsidies without breaching their bound rates or other relevant WTO disciplines.

In this context it has become more urgent for the WTO to strengthen multilateral disciplines that will reduce the scope for increased trade restriction, in particular to reach an early agreement in the Doha Round on Non-Agricultural Market Access (NAMA) and "modalities" for agriculture that will pave the way for agreement on other subjects that are under negotiation.

Commitments to Article XIV(2)[3] of the Marrakech Agreement establishing the WTO

To date, most members of the WTO appear to have successfully kept domestic protectionist pressures under control. From the TPRM report there is only limited evidence of increases in tariffs and non-tariff barriers, or of increased resort to trade remedy actions. The most significant actions taken, mainly in Organisation of Economic Cooperation and Development (OECD) countries, in response to the financial crisis and onset of economic recession, has involved financial support of one kind or another to banks and other financial institutions and to certain industries, notably the automobile industry. In mid-December 2008, the G-20, Asia Pacific Economic Cooperation (APEC), China, Japan and the Republic of Korea, at Heads of State level, pledged to refrain over the next 12 months from raising new barriers to trade and investment, imposing new export restrictions, or implement WTO inconsistent measures to stimulate exports.

For Article XIV (2) to be relevant and useful, monitoring of concessions and obligations needs to be evaluated at regular intervals and based on accurate information that is as comprehensive as possible. The delays by WTO members in notifying the changes in

[1] Contribution by Mr. G. Mqambalala is an Assistant Economist - Directorate: International Trade, Department of Agriculture

[2] An annual overview of developments in the international trading environment impacting on the multilateral trading system will also be undertaken by the TPRB. The overview is to be assisted by an annual report by the Director-General setting out the major activities of the WTO and highlighting significant policy issues affecting trade.

[3] Members who accept these Agreements after their entry into force shall implement those concessions and obligations in the Multilateral Trade Agreements that are to be implemented over a period of time, starting with the entry into force of these agreements as if they had been accepted on the date of their entry into force.

their respective applied tariff rates to the Integrated Data Base distort the application of Article XIV.2.

Macroeconomic and trade developments during the third quarter of 2008

The financial crisis occurred at a time when economic growth was already showing signs of slowing down, particularly in the OECD countries. Dollar prices played a much larger part in the value changes than in the volume changes. This implies that the changes are less dramatic in respect of output and employment than the nominal trade figures might suggest. In the first half of 2008, dollar trade values were boosted by the rise in commodity prices, most prominently by those of oil and food. In the second half, prices of fuels and food decreased sharply. The dollar depreciated sharply in the first half of 2008 against the currencies of major traders but appreciated against many in the second half (especially *vis-à-vis* the Euro). By December, oil prices had fallen to their lowest level in three years, and were 70 % down from their monthly peak level in 2008.

In its recent report on Global Economic Prospects 2009, the World Bank, like UNCTAD, marked its estimates of growth in 2008 and its forecast for 2009 down sharply. Of particular interest is the World Bank's forecast of a drop in global export volumes of -2.1 % in 2009, the first decline since 1982. Net private debt and equity flows to developing countries are projected to decline from $ 1 trillion in 2007 to about $ 530 billion in 2009, or from 7.7 % to 3 % of developing countries' GDP, contributing to a projected dramatic slowdown of investment growth in developing countries. In its recent World Investment Report 2008, UNCTAD had already estimated a 10 % decline in Foreign Direct Investment (FDI) flows in 2008, with developing countries being the most affected[4]. Other factors identified by the World Bank as contributing to slower growth in some developing countries are reduced remittance flows from migrant workers abroad[5], further falls in commodity prices and a slower growth of global tourism, which the World Tourism Organisation projects at between 0 % and 2 %, respectively, in 2009.

Projections for 2009 are sensitive to the assumption that the coordinated monetary and fiscal stimulus packages that were called for by the G-20 in mid-December to stimulate global demand will be effective. Several countries have introduced new economic stimulus packages in recent months (e.g. the US, Belgium, Switzerland, etc). South Africa's perceived massive job losses as the global credit crisis starts to bite could get relief from the R 10-billion package being put together by the government, business and labour. This could cushion the country from the effects of the financial meltdown. The industries likely to benefit from packages are the clothing, textile and footwear sector, the automotive and parts industry, capital equipment, retail, housing and private services. Despite the unpleasant job losses incurred, cost cutting drives that translate to retrenchments are already taking place in sectors such as mining in South Africa.

On the monetary side, major central banks have cut interest rates sharply and continue to inject significant amounts of liquidity into financial markets. Even though South Africa is in good shape it is not immune to the financial meltdown, and has seen its central bank cut repo rates by 50 basis points and 100 basis points in December 2008 and February 2009 respectively.

On the fiscal side, the IMF has proposed the need for additional stimulus of around 2 % of world GDP ($ 1.2 trillion), with major surplus countries encouraged to take a leading role. To date, new fiscal stimulus packages (separate from financial bailout packages) have been implemented or announced by, *inter alia*, the E.U., Japan and the U.S., Argentina, Chile, China, Indonesia, Malaysia, Mexico and Thailand. However, it is too early to appreciate the full implications of stimulus packages for trade *per se* or how they might be implemented through the procurement activities of various governments.

The economies of all WTO Members will be affected by the economic slowdown in 2009, but the forecasts of weaker economic growth for developing countries are of particular importance, because for many of them growth is heavily dependent on exports of commodities which are currently exhibiting a fall in demand. In addition, decelerating trade growth has become the main downward driver of world economic growth for these countries, even more so than domestic demand.

Given the fact that South Africa is part of globalisation, one has to ask these questions: Is trade growth, and export growth in particular, the main driver of economic growth for the South African economy? What percentage do import consumption and foreign direct investment contribute to our economic growth? What percentage does domestic consumption and domestic investment contribute to our economic growth? The extreme vulnerability of the global economy to trade developments clearly illustrates the perils of trade protectionism in current circumstances. An important issue that could have implications for the use of trade measures will be how macroeconomic imbalances of countries around the world, particularly external imbalances and exchange rates, are affected by these stimulus packages and by an environment in which the availability of external financing is considerably reduced.

Trade policy related developments in Agriculture

As noted earlier, there has been only limited evidence so far of increases in tariffs or non-tariff barriers, or increased resort to trade remedy actions. Even though some member countries have put their needs before those of the international trading community, their trade policy related development measures re-

[4] According to the World Association of Investment Promotion Agencies, worldwide FDI is expected to fall by 12-15 % in 2009 due to the financial crisis.

[5] In 2006, worker remittances exceeded 10 of GDP in at least 24 countries (World Bank data).

main consistent with their concessions and obligations. The following information about trade policy related developments on agricultural measures was collected subsequent to the outbreak of the financial crisis in September 2008. According to the WTO Secretariat JOB (09)/2:

- Mercosur members reached an agreement in November 2008 to raise their common external tariff by five percentage points on average, on a number of items including wine, peaches and dairy products. However, this agreement was not ratified at Mercosur's Summit in mid-December 2008.
- On 20 October 2008, Brazil's Central Bank issued US$ 1.62 billion in six-month loans in an attempt to provide relief to exporters, especially in the farming sector.
- On 26 November 2008, Ecuador reportedly raised its tariffs on 940 products, including butter, turkey, crackers, caramels, etc. by between 5 and 20 percentage points. As a result, Ecuador expects to collect additional revenues of US$ 85.5 million. According to the authorities, the tariff increases aim to reduce the impact of the financial crisis and take Ecuador's WTO commitments into account.
- Since 15 December 2008 only five ports and certain international airports in Indonesia are to serve as entry points for certain imports, including food and beverages.
- The European Commission has announced the re-introduction of export subsidies for butter, cheese, and milk or other milk products from late January 2009.
- As part of its stimulus plan, Argentina has reportedly cut its export taxes on wheat and corn by five percentage points to 23 and 20, respectively.
- Indonesia announced measures to facilitate trade by using a centralised electronic system for customs declarations at two key ports.
- As part of its programme to simplify foreign trade between 2009 and 2013 Mexico announced that it will reduce tariffs on about 80 % of manufactured goods imports from countries with which it has no preferential trade agreement.
- In December 2008 Russia's proposed legislation to provide for increases in export duties on wood was temporarily delayed, although not repealed. Sanitary and Phytosanitary (SPS) measures and quarantine requirements have continued to increase. Meat import quotas have been reduced. Furthermore, new trade-related investment measures and export subsidies have been introduced.
- The South African International Trade Administration Commission[6] (ITAC) zero-rated the 2 % blanket import duty on wheat in February 2009.

This economic volatility has spread quickly to emerging market economies and other developing countries through sharp falls in export demand, foreign investment and commodity prices, as well as the effects of the global shortage of credit on their economies, including shortages of trade finance. Moreover, the sharp deterioration of global economic prospects is triggering a general re-assessment of credit risk, entailing a sharp increase in the cost of credit, insurance, and guarantees for trade operations, with developing countries and Least Developed Countries being most affected. The agricultural sector is greatly affected, which makes the revival of the Doha round even more important.

1.2 SOUTH AFRICA'S AGRICULTURAL TRADE RELATIONS WITH INDIA[7]

The objective of this section is to probe South Africa's agricultural trade engagement with India and explore opportunities for South Africa's agricultural exports. While the current trade talks with India are still underway, and the outcome thereof with respect to improved market access for the agricultural sector therefore uncertain, it is prudent to start planning new investments and production adjustments should a major boost in demand occur as a result.

India's economy has had positive growth rates from 2003 to 2008. Between 2001 and 2007, real GDP growth averaged above 7 % per annum. In the fiscal year 2006/07 it rose to 8.4 %. The leading growth sectors are services and manufacturing. Employment in these sectors has contributed to the increased population of young, middle-income urban dwellers.

Indian consumers contribute significantly to a growing global demand for food. This is accompanied by changing consumption patterns, e.g. an increase in consumption of meat, milk and eggs, which has led to increased demand for grain and oil seeds for production of animal feed. These features, together with increased demand for Western-style and fast foods, present potential markets for South African agricultural products, particularly value added and high valued food items.

The export potential is combined with challenges:

- Non-tariff barriers (NTBs) such as import permits and state trading;
- Complex SPS requirements and technical barriers to trade (e.g. labelling);
- A protective tariff regime with the majority of tariffs at their bound rates; and
- Costs of transaction and regulatory constraints, which impede access to the Indian agricultural market.

[6] ITAC (http://www.itac.org.za/docs/import-tariffs-wheat-3feb2009.pdf)

[7] Contribution by Moses Sphamandla Mazibuko & Zithulele Balindlela, Directorate International Trade, Department of Agriculture. Information and data sources: India's Trade Policy Review documents of 2007, and World Trade Atlas 2008 for statistical data.

This is reflected in the growing trade deficit between South Africa and India.

Current trade flows between South Africa-India

South Africa's share of agricultural exports to India declined from 0.8 % in 2007 to 0.56 % in 2008, with India being ranked 41st as market for South African exports. On the other hand, India is ranked 13th as South Africa's supplier of agricultural imports, even though its share in South Africa's imports dropped from 4.67 % in 2007 to 2.91 % in 2008. South Africa is ranked at 39th position by India as a supplier, with a share of 0.3 % in 2008. The table in Appendix A summarises the top 5 agricultural commodities traded between the two countries in 2007 and 2008.

- Wool is South Africa's leading agricultural export to India. Its share in total agricultural exports to India increased from 46 % in 2007 to 63 % in 2008, while that of the main import product (rice) dropped from 53 % in 2007 to 35 % in 2008. Both the diversity and quantity of South Africa's exports declined over the past year.
- South Africa has the potential to export dairy products, vegetables and fruits and increase wine exports to India. These are products that India is importing from the rest of the world and which South Africa exports competitively to the world, but not to India.

In conclusion, changing consumption patterns, increasing demand for food, higher incomes and positive economic growth all favour potential exports by South Africa to India, but the Indian market remains difficult to access in the absence of a trade arrangement. In view of the above challenges, South Africa, as a member of SACU, is negotiating a preferential trade agreement with India to improve market access. The scope of the negotiations involves both tariffs and non-tariff barriers.

1.3 THE SOUTH AFRICAN FOOD INFLATION LINK WITH CHINESE FOOD IMPORTS[8]

While many factors contributed to the recent global food price increases, the steadily increasing role of China in agricultural global trade is generally accepted as being one of these factors. A recent Tralac publication (2008) examines the link between food inflation in South Africa and agricultural food imports into China. The indications are that increasing Chinese imports are one of the factors behind rising global food prices, which in turn have a direct impact on South African import prices, and consequently domestic food prices. Table 1 shows the aggregate food price index and the comparable indices for meat, dairy, cereals, oils and sugar. Table 2 shows the global food price index from July 2007.

Table 1: Global food price index, 1998-2000 =100

Index	Food	Meat	Dairy	Cereals	Oils	Sugar
2000	92	100	106	85	72	105
2001	94	100	117	87	72	111
2002	93	96	86	95	91	88
2003	102	105	105	99	105	91
2004	114	118	130	108	117	92
2005	117	121	145	105	109	127
2006	127	115	138	123	117	190
2007	156	121	247	169	174	129

Table 2: Global food price index - from July 2007

	Food	Meat	Dairy	Cereals	Oils	Sugar
July 07	155	120	277	157	175	131
Aug	161	123	287	168	181	126
Sept	170	124	290	191	190	125
Oct	174	122	297	197	202	128
Nov	179	126	302	199	221	130
Dec	186	123	295	220	226	137
Jan 08	196	126	281	235	250	154
Feb	215	128	278	278	273	173
March	218	132	276	277	285	169
Apr	215	132	266	278	276	161
May	215	141	265	270	280	155
Jun	219	144	263	273	292	156
July	213	144	265	256	274	183

Source: FAO data at http://www.fao.org/worldfood situation/FoodPricesIndex/en/

In July 2008 the price indices for dairy, cereals and oils represented the highest increase when compared to 2000. Figures 1 and 2 show the increase in prices of oils and cereals, the main agricultural commodities imported by South Africa and China respectively.

[8] Contribution by Ms J Lanecki, Directorate International Trade, Department of Agriculture. This section was compiled using information from the following sources: Tralac, NAMC, USDA, World Trade Atlas and StatsSA

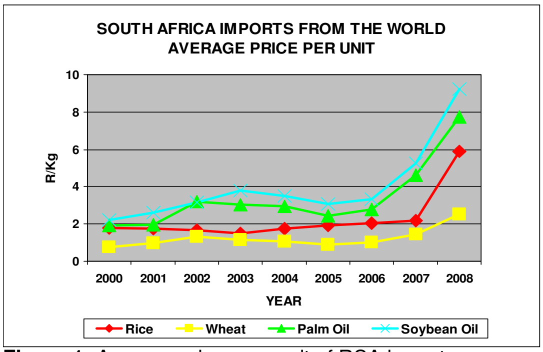

Figure 1: Average prices per unit of RSA imports

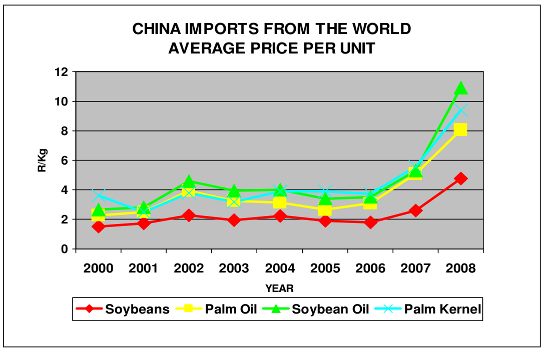

Figure 2: Average prices per unit of Chinese imports

China's trade pattern in agricultural commodities follows its comparative advantage: It tends to import land-intensive commodities (soybeans, cotton, barley, plant oils) and it exports labour intensive commodities (fish, fruits, vegetables and processed agricultural goods). China is also a major exporter of maize in most years.

In 2008 China's agricultural imports totalled an estimated US$ 57 billion, and its agricultural exports US$ 29 billion. During the same period South Africa's agricultural imports totalled approximately US$ 3.8 billion and exports US$ 4.4 billion.

Tralac's analysis indicates that Chinese agricultural imports for the first six months of 2008 increased by over 65 % when compared to the first six months of 2007. The main components of those imports were various seeds, grains, fats and oils, which are also important imports into South Africa. The weighted average price increase for agricultural products imported to China was almost 54 %(the sample of the top 25 import lines). The major increase comprised of soybeans, palm oil, barley, rape oil, palm kernel oil, vegetable fats, and pork meat.

Over the same periods (January to the end of June 2007 and 2008) the weighted average price increase per unit for the main agricultural imports into South Africa was just over 49 % when adjusted to represent the full import values. Nearly half of this increase (21) was driven by the large average increases in the top four lines: rice, wheat, palm oils and soya beans. At the same time, there was a less than 10.5 % average price increase in the top 25 export lines from South Africa to the world over the same period. This means that during the period the analysis covered (global commiduty boom) the big influence on South Africa was through its agricultural imports and not through its export commodities. Therefore South Africa imported the wrong commodities and exported the wrong commodities to reap the full benefit of the commodity boom.

Chinese food imports are having a significant impact on South African import prices in several of the top import lines, while at the same time there is little Chinese demand effect coming through to benefit South African exports. Food inflation remains one of the major drivers of overall inflation in South Africa. Rising food prices continue to threaten household food security of the poor in South Africa. Although the South African economy is expected to grow at a slightly higher pace later this year, economic growth is likely to remain under pressure. Consumer expenditure is also expected to remain under pressure due to high interest rates, high fuel costs and high food prices.

Appendix A:

Top 5 agricultural exports and imports - SA and India

SA exports to India in million Rands				**SA imports from India in million Rands**			
Product	**EXv 2008**	**India's share of total export (%)**	**Competitors**	**Product**	**IMv 2008**	**India's share of total import (%)**	**Competitors**
Wool	159.3	13.9	Australia	Rice	392.9	10.6	Thailand
Cane sugar	39.0	3.8	Denmark	Tobacco	90.5	12.4	Zimbabwe
Pears & quinces	9.7	1.1	China	Soybean oil cake	74.5	2.9	Argentina
Dog & cat food	6.6	8.1	New Zealand	Roasted chicory	48.7	98.6	USA
Seeds, fruit, spores	4.8	9.6	Australia	Cane molasses	38.1	44.0	Zimbabwe